OMNICARE Health Plan SM

First Amendment to Rehabilitation Plan
June 2002

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Introduction

Under the March 2002 proposed Rehabilitation Plan for OmniCare Health Plan ("OmniCare") or ("Health Plan") previously filed with the Ingham County Circuit Court ("Court"), the debt restructuring approach included therein entailed the largest individual creditor receiving no cash and having its entire liability restructured into surplus notes. In order to implement the contemplated debt restructuring, an agreement on the terms of the surplus notes was required. The creditor and the Commissioner were unable to reach an acceptable agreement, and accordingly, on May 23, 2002, the Commissioner advised the Court that he would submit a First Amendment to the Rehabilitation Plan. This First Amendment to the Rehabilitation Plan addresses only amended areas and relevant additional information to the proposed Rehabilitation Plan.

Debt Restructuring

Under the First Amendment to the Rehabilitation Plan, all creditors will be paid in cash for pre-rehabilitation liabilities at varying percentages on the dollar. These percentages are in some cases lower than the percentages included in the original proposed Plan. The lower percentages are required for the additional cash necessary for all creditors, including the largest creditor, to have an option of receiving cash as full settlement for their claims. Under the revised plan, each creditor will have two payment options from which to choose:

A. Cash payment; or,
B. Reduced cash payment coupled with a surplus note for the balance of the creditor's claim

Under Option A, each creditor will be paid in cash at the applicable percentage for a total discharge of its debt. Under Option B, applicable un-subordinated creditors will receive cash payments discounted 10% on the dollar from the corresponding payment under Option A plus surplus notes for the remainder of their outstanding claim. Creditors will hold surplus notes issued under Option B until OmniCare is in full statutory compliance and the Office of Financial and Insurance Services ("OFIS") approves payment on the notes from surplus earnings. If OmniCare pays the principal of the surplus notes in full at any time during years one through seven after the date of issuance, the principal shall be paid at an amount equal to the following applicable percentages of the unpaid principal:

Loan Year	Applicable Repayment % of Principal
2003	30%
2004	40%
2005	50%
2006	60%
2007	70%
2008	80%
2009	90%

Upon payment of the note at the applicable rate above, the note will be paid in full. The objective of discounting the principal is to provide each creditor with an appropriate return on selection of Option B based upon the time elapsed between note issuance and repayment, and in consideration of the decreased initial cash payment. A sample of the surplus note form that will be used for creditors electing Option B is included as Attachment A.

Individually large hospital providers[1] that choose Option A will be paid over time at a rate 5% higher than other hospitals electing Option A. The higher rate compensates them for the time value resulting from payment to those creditors in installments. Individually large providers paid under Option A will receive installment payments according to the following schedule:

[1] Individually large hospital providers include the Detroit Medical Center and Henry Ford Health System.

Payment Due Date	Portion of Total Payment
On or before September 1, 2002	50%
On or before September 1, 2003	25%
On or before September 1, 2004	25%

A summary of the cash payout percentages under Options A and B as compared to the previously proposed debt-restructuring plan is indicated below:

Class	Previous Plan	Payment Option A	Payment Option B*
Subscribers	100%	100%	N/A[2]
Physician and Non-Physician Medical Providers	55%	45%	35%
Individually Large Hospital Providers	0-35%	35%	25%
Hospitals	35%	30%	20%
Pay In Full Providers	25%	25%	15%
Pharmacy	25%	25%	15%
Primary Care Centers	25%	25%	15%
Collection Agencies	0%	0%	N/A[3]
Primary Care Capitation Withhold	25%	25%	15%
Federal Government	55%	20%	10%
Surplus Notes (subordinated creditors)	0%	0%	N/A[4]

*Option B does not include a value for the surplus note

If OmniCare were liquidated, non-subordinated creditors would receive approximately $0.26 on the dollar of pre and post-rehabilitation debt. Conversely, the First Amended Rehabilitation Plan provides for the average non-subordinated creditor to receive approximately $0.52 on the dollar of pre and post-rehabilitation debt (on a weighted average basis).

[2] Option not applicable since class is paid at 100%.
[3] Option not applicable since the underlying medical liabilities are appropriately handled under the appropriate provider class.
[4] Option not applicable since this pre-petition debt is subordinated to all other creditors and will not be re-issued under the First Amended Rehabilitation Plan.

Depending on the creditor elections of Option A or B, the First Amended Rehabilitation Plan calls for a total cash payout to creditors ranging from $17.5 to $24.4 million dollars for pre-rehabilitation debt. Additionally, up to $50.2 million in debt could be converted to surplus notes under Option B. Upon restructure of the debt, OmniCare will have an increase in net worth ranging from approximately $43.4 to $50.2 million dollars. Once the Rehabilitation Plan is approved and creditor elections have been made for either Option A or Option B, cash payouts, for creditors other than individually large hospitals, are projected to be completed within thirty days (30). The revised Debt Restructure Table summarizing the overall impact of the debt restructuring is included as Attachment B.

Medical Claim Liabilities

A revised schedule of medical claim liabilities incorporating the calculation of payments to creditors under the First Amended Rehabilitation Plan is included as Attachment C. The "look back" approach outlined in the proposed Rehabilitation Plan is consistently applied herein. A narrative description of each column heading of Attachment C is included as Attachment D. Under the First Amended Rehabilitation Plan, an additional step was taken to sort the file by tax identification number and offset positive and negative restated "look-back" amounts against one another for providers with multiple vendor numbers and/or multiple tax identification numbers.

Capitation Withhold

A revised schedule of capitation withhold liabilities as of July 30, 2001 incorporating the calculation of payments to creditors under the First Amended Rehabilitation Plan is included as Attachment E.

Federal Government-Employer Group

OmniCare has had a contract with the FEHBP since its approval for participation in 1979. Under this employer group contract, Plans are required by law to offer the FEHBP premium rates that are at or lower than the rates offered to the two groups closest in size to the FEHBP (SSSG's), adjusted for benefit differences. The development of rates for the FEHBP and the SSSG's are subject to review and audit by the United States Office of Personnel Management (OPM) in order to ascertain that the rates adhere to the legal criteria. Pursuant to a settlement agreement with the OPM for an audit of the rate development for the years 1988-1992, OmniCare has an outstanding balance of $231,566 due to the Federal government. Additionally, OmniCare has recently undergone an audit of the years 1996-2000 for which OmniCare has recorded a contingent liability of $2.3 million for potential amounts due to OPM related to the rate development of those years.

Under the proposed Rehabilitation Plan, liabilities pursuant to OmniCare's contract with the FEHBP were treated with a higher rank in percentage under the assumption that in a liquidation, the debt would be treated in a class above other creditors. A percentage reduction is necessary to correct this assumption under the First Amended Rehabilitation Plan and to reflect a lower percentage consistent with other creditors.

Surplus Notes

As of July 30, 2001, OmniCare had surplus notes outstanding in the amount of $17.3 million. Since surplus notes are subordinated to all other creditors who are receiving less than 100% on the dollar as proposed hereunder, it is proposed and justifiable to reimburse surplus notes at 0% since obligations senior to the surplus notes would be settled at a discount under the proposed amendment.

<u>Pending Lawsuits</u>

OmniCare has four (4) open litigation files, as follows:

Outstanding Legal Cases

Claimant	Basis	Claim Amount
Total Family Health Services, PC vs. Michigan HMO Plans d/b/a/OmniCare Health Plan	Reimbursement for Legal Fees	$130,000
Henry Ford Hospital vs. Edna Scott vs. Prudential Ins and OmniCare	COB Case Auto Insurance	$8,421
Nadia Solomon-Searcy vs. Auto Owners Insurance Company and OmniCare Health Plan	COB Case Auto Insurance	Approximately $25,000
Wakeker Blinks vs. Michigan HMO Plans d/b/a/OmniCare Health Plan	COB Case	$39,569

Consistent with the proposed Rehabilitation Plan, no additional payments will be made under the First Amendment to the Rehabilitation Plan. Additionally, Option B is not applicable due to the proposed discharge of these actions as summarized in the proposed Rehabilitation Plan.

Financials

- **December 31, 2001 Financials**

KPMG audited the statutory financial statements of OmniCare as of December 31, 2001. A copy of this report is included as Attachment F. As indicated in the previously filed Rehabilitation Plan, KPMG had previously disclaimed an opinion on the Health Plan's December 31, 2000 financial statements citing an inability to perform sufficient procedures on the Health Plan's accounting records to gain comfort regarding the fair statement of medical liabilities. Subsequent to the initiation of rehabilitation by OFIS, substantial improvements were made to the Health Plan's accounting records and an actuarially sound claims development model has been implemented. As a result of the improvements made in financial reporting and controls, the December 31, 2000 financial statements were restated and KPMG's disclaimer was removed based upon KPMG's ability to gain sufficient comfort regarding the fair statement of medical liabilities as reported by the Health Plan. Additionally, the requisite actuarial opinion was obtained from the consulting actuary certifying the accuracy of the medical claims liability as of December 31, 2001. The December 31, 2001 audited statutory financial statements continue to carry a disclaimer of opinion due to the material uncertainty of OmniCare as a "going concern" which is a requirement under statutory accounting and auditing guidance given OmniCare's current capital deficiency. It is important to note, however, that the disclaimer is no longer related to a deficiency in the accounting records.

- **Financial performance August 2001 through March 2002**

While the audited statutory financial statements for the year ended December 31, 2001 indicate a loss of $17.5 million for the year, this loss is made up of a $20.5 million loss in the seven months prior to the rehabilitation order and a $3 million surplus in the five-month post-rehabilitation period, after proper classification of pre and post rehabilitation operations.

Favorable operations have continued in 2002 with a $678,000 surplus for the first quarter. It should be noted that first quarter operating results include one-time adjustments for the estimated costs associated with winding down operations of a joint venture. The March 31, 2002 internal financial statements (balance sheet and income statement) have been included as Attachment G. The substantive changes driving the post-rehabilitation financial turnaround are a substantial reduction in administrative costs, investment in, and implementation of necessary medical management policies and procedures, stabilization of claims processing operations, increased commercial premium rates along with strict adherence to underwriting and rating philosophy and guidelines, capitation of hospital costs for approximately 49% of the Health Plan's membership and improvement of coordination of benefits policies and procedures.

- **Statutory Capital Projections**

The current HMO reserve requirements stipulating an HMO to a minimum $500,000 in positive net worth has been repealed. The revised requirements that go into effect December 31, 2003 require that HMOs must maintain a minimum net worth equal to the greater of 4% of annualized revenue, three months uncovered expenditures, or $1.5 million. Based on OmniCare's 5-year projections, the minimum net worth requirement is $9.2 million.

OmniCare has not been in compliance with the reserve requirements of OFIS. This factor was the substantive deficiency driving its petition to place the Health Plan into rehabilitation. Coupled with a strategy to convert OmniCare to a for-profit organization, a 5-year projection was completed to determine the anticipated timeframe for meeting statutory capital requirements and to establish an estimated enterprise for the company. The 5-year projections were included in the proposed Rehabilitation Plan. Statutory capital projections are included as Attachment H to reflect the impact of the debt restructuring under the First Amendment to the Rehabilitation Plan.

Medicaid Contract Extension Update

On April 30, 2002, the Department of Community Health renewed OmniCare's Medicaid contract for another two years, expiring October 1, 2004. A copy of the letter of extension is included as Attachment I.

Implementation Schedule

This *restoration* period will consist of disbursement of the provider payments based on the approved First Amended Rehabilitation Plan, executing surplus notes as necessary, converting the organization to for-profit, seating of the Board of Directors, converting the organization to a director company, relocating the corporate offices, converting the staff to OmniCare employees, planning and implementing the information systems strategies and continuing to focus on improving the existing organization.

As a result of the additional time elapsed from the need to amend the proposed Rehabilitation Plan, the following represents the revised projected timeframes:

Implementation Schedule[5]

Task	Completion Date
• 90-Day termination notice to UAHC	August 1, 2002
• Relocation of corporate offices	November 1, 2002
• Plan system strategy	July 1, 2002
• Convert Personnel to OmniCare	November 1, 2002
• Install Systems Solution	January 1, 2003
• Disbursement of cash: Rehabilitation Plan	September 1, 2002
• Conversion to for-profit	January 1, 2003
• Installation of a Board of Directors	January 1, 2003

Recommendations

Therefore, the Ingham County Court is being petitioned for the following:

- Approve the Rehabilitation Plan as amended and submitted;
- Order that the reimbursement rate for Medicaid providers of OmniCare be at the Medicaid rates as periodically modified by the State of Michigan; and
- Continue the Order For Injunctive Relief issued on by this Court until Rehabilitation is terminated.

[5] Note: The above assumes the First Amended Rehabilitation Plan is approved as submitted prior to the end of July 2002.